

Auditor-General of South Africa

Msunduzi Municipality and its
municipal entity - Audit report 2016-17

Report of the auditor-general to the KwaZulu-Natal Provincial Legislature and the council on Msunduzi Municipality and its municipal entity

Report on the audit of the consolidated and separate financial statements

Disclaimer of opinion

1. I was engaged to audit the consolidated and separate financial statements of Msunduzi Municipality and its municipal entity set out on pages ... to ..., which comprise the appropriation statement, the consolidated and separate statement of financial position as at 30 June 2017, the consolidated and separate statement of financial performance, statement of changes in net assets, consolidated and separate cash flow statement and statement of comparison of budget and actual amounts for the year then ended, as well as the notes to the consolidated and separate financial statements, including a summary of significant accounting policies.
2. I do not express an opinion on the consolidated and separate financial statements of the municipality and its municipal entity. Because of the significance of the matters described in the basis for disclaimer of opinion section of this report, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these consolidated and separate financial statements.

Basis for disclaimer of opinion

Land and buildings - Restatement of corresponding amounts

3. I was unable to obtain sufficient appropriate audit evidence for the restatement of the corresponding amounts for land and buildings included in property, plant and equipment in the consolidated and separate financial statements. As described in note 13 to the consolidated and separate financial statements, the restatement was made to rectify a previous year misstatement, but it could not be substantiated by supporting audit evidence. I was unable to confirm the restatement by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to the land and buildings stated at R1,47 billion in the consolidated and separate financial statements.

Property, plant and equipment - Other assets

4. I was unable to obtain sufficient appropriate audit evidence that management, had properly accounted for other assets included in property, plant and equipment, as they could not be verified. I was unable to confirm these assets by alternative means. Consequently, I was unable to determine whether any further adjustment relating to other assets stated at R408,74 million as disclosed in note 13 to the consolidated and separate financial statements were necessary.

Investment property – Restatement of corresponding amounts

5. I was unable to obtain sufficient appropriate audit evidence for the restatement of the corresponding amounts for Investment property in the consolidated and separate financial statements. As described in note 12 to the consolidated and separate financial statements, the restatement was made to rectify a previous year misstatement, but it could not be substantiated by supporting audit evidence. I was unable to confirm the restatement by alternative means. Consequently, I was unable to determine whether any adjustment was necessary to the investment property stated at R720,22 million (2016: R591,24 million) in the consolidated and separate financial statements.

Revenue from exchange transactions

6. I was unable to obtain sufficient appropriate audit evidence for revenue from exchange transactions which was presented for audit purposes without the underlying supporting ledgers. I was unable to audit the revenue from exchange transactions by alternative means. Consequently, I was unable to determine whether any adjustments to revenue from exchange transactions stated at R2,73 billion disclosed in notes 28 - 31 and 33 - 35 to the consolidated and separate financial statements were necessary.

Revenue from non-exchange transactions

7. I was unable to obtain sufficient appropriate audit evidence for revenue from non-exchange transactions which was presented for audit purposes without the underlying supporting ledgers. I was unable to audit the revenue from non-exchange transactions by alternative means. Consequently, I was unable to determine whether any adjustments to revenue from non-exchange transactions stated at R795,88 million disclosed in note 36 to the consolidated and separate financial statements were necessary.

Consumer debtors

8. I was unable to obtain sufficient appropriate audit evidence as consumer debtors recorded in the consolidated and separate financial statements did not reconcile to the debtors age analysis. I was unable to confirm consumer debtors stated at R2,08 billion in note 4 to the consolidated and separate financial statements by alternative means as it was impracticable to do so. Additionally, there was a resultant impact on the related revenue and impairment that could not be determined.

Receivables from exchange transactions

9. I was unable to obtain sufficient appropriate audit evidence that receivables from exchange transactions was properly accounted for due to the status of accounting records for prepayments disclosed. I was unable to confirm these prepayments by alternative means. Consequently, I was unable to determine whether any adjustments to receivables from exchange transactions stated at R51,37 million (2016: R111,89 million) disclosed in note 7 to the consolidated and separate financial statements were necessary. Additionally, there was a resultant impact on the related impairment in note 52 that could not be determined.

Expenditure - Bad debts written off

10. Management had written off consumer debts without the appropriate council resolution as required by section 64(2)(a) of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA). Furthermore, bad debts written off were not adequately supported. I was unable to confirm the bad debts written off by alternative means. Consequently, I was unable to determine whether any adjustments relating to bad debts written off stated at R332,29 million in note 40 to the consolidated and separate financial statements were necessary. Additionally, there was a resultant impact on the related consumer debtors which could not be determined.

Commitments

11. Management did not properly account for commitments as required by SA Standards of GRAP 17 *Property, plant and equipment* due to inadequate systems and processes to account for this disclosure. I was unable to determine the full extent of the misstatement as it was impractical to do so. Consequently, commitments stated at R286,94 million in note 60 to the consolidated and separate financial statements was misstated by an unknown amount.

Inventory

12. Management did not disclose the change in the inventory accounting policy in terms of South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) 3, *Accounting policies, estimates and errors*. The nature and the amount of the correction at the beginning of the earliest previous period were not disclosed as supporting information was not provided. Additionally, adjustments were made to inventory which could not be supported. I could not confirm these adjustments nor the impact of the change of accounting policy by alternative means. Consequently, I was unable to determine whether any adjustments to inventory stated at R66,14 million disclosed in note 5 to the consolidated and separate financial statements were necessary.

Emphasis of matters

13. I draw attention to the matters below.

Material underspending of the conditional grant

14. As disclosed in note 38 to the consolidated and separate financial statements, the municipality materially underspent the budget on the public transportation infrastructure grant and the neighbourhood development partnership grant due to the delays in the implementation of the projects associated with these grants. As a result of the material underspending, the municipality surrendered R165,18 million and R29,77 million to National Treasury respectively.

Material losses – electricity

15. As disclosed in note 70 to the consolidated and separate financial statements, material electricity losses of R279,12 million (2015-2016: R 181,96 million) was incurred, which represents 16% (2015-2016: 12%) of total electricity purchased. Losses were as a result of illegal connections.

Other matters

I draw attention to the matters below:

Unaudited disclosure notes

16. In terms of section 125(2)(e) of the MFMA the municipality and its municipal entity are required to disclose particulars of non-compliance with the MFMA in the consolidated and separate financial statements. This disclosure requirement did not form part of the audit of the consolidated and separate financial statements and accordingly I do not express an opinion thereon.

Unaudited supplementary schedules

17. The supplementary information set out on pages xx to xx does not form part of the consolidated and separate financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion thereon.

Responsibilities of the accounting officer for the consolidated and separate financial statements

18. The accounting officer is responsible for the preparation and fair presentation of the consolidated and separate financial statements in accordance with the SA Standards of GRAP, and the requirements of the MFMA, and Division of Revenue Act of South Africa,

2016 (Act No. 3 of 2016) (DoRA) and for such internal control as the accounting officer determines is necessary to enable the preparation of consolidated and separate financial statements that are free from material misstatement, whether due to fraud or error.

19. In preparing the consolidated and separate financial statements, the accounting officer is responsible for assessing the municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the intention is to liquidate the municipality and its municipal entity or cease operations, or there is no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the consolidated and separate financial statements

20. My responsibility is to conduct an audit of the consolidated and separate financial statements in accordance with the ISAs and to issue an auditor's report. However, because of the matters described in the basis for disclaimer of opinion section of this report, I was not able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion on these consolidated and separate financial statements.
21. I am independent of the municipality and its municipal entity in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) and the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.

Report on the audit of the annual performance report

Introduction and scope

22. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof I have a responsibility to report material findings on the reported performance information against predetermined objectives for the selected objectives presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.
23. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance measures included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
24. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected objectives presented in the annual performance report of the municipality and its municipal entity for the year ended 30 June 2017:

Objectives	Pages in the annual performance report
Basic service delivery	x – x
Cross cutting issues (Safe City Msunduzi NPC)	x – x

25. I performed procedures to determine whether the reported performance information was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
26. The material findings in respect of the usefulness and reliability of the selected objectives are as follows:

Basic service delivery

Various indicators – Performance indicators not specific

27. The targets as determined during planning for the indicators listed below were not specific in clearly identifying the nature and required level of performance, as required by the Framework for managing programme performance information (FMPPPI).

■ Number of libraries maintained ■ Number of operational halls maintained every month ■ Date manufacturing process of 1 X 13-panel 11kV switchboard for new 132/11kV East Wood substation completed ■ Date manufacturing process of 28 X 11kV fixed pattern switchgears for 3 distributor substations completed ■ Date Leachate tank commissioned ■ Metres of berm constructed and height.

Various indicators – Performance indicators not verifiable and reliable

28. I was unable to obtain sufficient appropriate audit evidence for the reported achievement of targets. This was due to a lack of proper performance management systems and processes to maintain records to enable reliable reporting on achievement of targets. I was unable to confirm that the reported achievement of these indicators was reliable by alternative means. Consequently, I was unable to determine whether any adjustments were required to the reported achievement of the indicators listed below.

■ % Reduced total water losses (wards1-9) ■ % Reduced total water losses (wards10-37) ■ Number of households with access to refuse removal at least once per week (wards 10 -37). ■ Number of New Electricity connections completed (Number of households with access to electricity) ■ Number of New Water connections completed (Application Driven) (Number of households with access to potable (drinkable) water) ■ Number of households earning less than R3500 per month (application based) provided with access to free basic services.

Number of HIV/AIDS and social support programmes to be coordinated – Reported achievement not complete

29. The reported achievement for the number of HIV/AIDS and social support programmes to be coordinated was misstated as the evidence provided indicated an estimated 685 and not 597 as reported.

Cross cutting issues

30. I did not raise any material findings on the usefulness and reliability of the reported performance information for the cross cutting issues objective.

Other matters

31. I draw attention to the matters below.

Achievement of planned targets

32. The annual performance report on pages x to x; x to x includes information on the achievement of planned targets for the year and explanations are provided for the under and overachievement of a significant number of targets. This information should be considered in the context of the material findings on the usefulness and reliability of the reported performance information in paragraphs 27 to 29 of this report.

Adjustment of material misstatements

33. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of the basic service delivery objective. As management subsequently corrected only some of the misstatements, I raised material findings on the usefulness and reliability of the reported performance information. Those that were not corrected are reported above.

Report on the audit of compliance with legislation

Introduction and scope

34. In accordance with the PAA and the general notice issued in terms thereof I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.
35. The material findings on compliance with specific matters in key legislation are as follows:

Annual financial statements

36. The consolidated and separate financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of disclosure items identified by the auditors in the submitted consolidated and separate financial statements were subsequently corrected and the supporting records were provided subsequently, but the uncorrected material misstatements and supporting records that could not be provided resulted in a disclaimed audit opinion.

Procurement and contract management

37. Goods and services with a transaction value of below R200 000 were procured without obtaining the required price quotations, in contravention of regulations 17(a) and (c) of the Municipal Supply Chain Management Regulation, 2005 (MSCMR).
38. Some of the invitations for competitive bidding at the municipality were not advertised for a required minimum period of days, in contravention of regulations 22(1) and 22(2) of the MSCMR. Similar non-compliance was also reported in the prior year.
39. Awards were made to providers who were in the service of the municipality and whose directors or principal shareholders are in the service of the municipality, in contravention of section 112(j) of the MFMA and MSCMR 44. Furthermore, the provider failed to declare that they were in the service of the municipality, as required by MSCMR 13(c).
40. Persons in the service of the municipality who had a private or business interest in contracts awarded by the municipality failed to disclose such interest, in contravention of

MSCMR 46(2)(e) and the code of conduct for staff members issued in terms of the Municipal Systems Act of South Africa, 2000 (Act No. 32 of 2000).

Expenditure management

41. Effective steps were not taken to prevent irregular expenditure of R150,21 million as disclosed in note 66 to the consolidated and separate annual financial statements, as required by section 62(1)(d) and 95(d) of the MFMA. The majority of the irregular expenditure was caused by non-compliance with supply chain management regulations.
42. Effective steps were not taken to prevent fruitless and wasteful expenditure of R11,27 million, as disclosed in note 68 to the consolidated and separate annual financial statements, in contravention of section 62(1)(d) of the MFMA. The majority of the disclosed fruitless and wasteful expenditure was caused by employee suspensions not finalised on time.

Revenue management

43. An adequate management, accounting and information system which accounts for revenue, debtors and receipts of revenue was not in place, as required by section 64(2)(e) of the MFMA.
44. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.

Asset management

45. An effective system of internal control for assets was not in place, as required by section 63(2)(c) of the MFMA.

Consequence management

46. Unauthorised, irregular and fruitless and wasteful expenditures were certified by council of the municipality as irrecoverable without having conducted an investigation to determine the recoverability of the expenditure, in contravention of section 32(2) of the MFMA.

Other information

47. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report which includes the mayor's foreword, executive summary, governance information, organisational performance, audit committee's report and other appendices. The other information does not include the consolidated and separate financial statements, the auditor's report and those selected objectives presented in the annual performance report that have been specifically reported in the auditor's report.
48. My opinion on the consolidated and separate financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
49. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated and separate financial statements and the selected objective presented in the annual

performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.

50. I did not receive the other information prior to the date of this auditor's report. When I do receive and read this information, if I conclude that there is a material misstatement therein; I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected, I may have to retract this auditor's report and re-issue an amended report as appropriate; however, if it is corrected this will not be necessary.

Internal control deficiencies

51. I considered internal control relevant to my audit of the consolidated and separate financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon.
52. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for disclaimer of opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

Leadership

53. Leadership did not adequately oversee financial and performance reporting and compliance with legislation. In this regard, leadership did not ensure that effective measures were taken to address previous findings to support the achievement of credible reporting and compliance with legislative requirements.

Financial and performance management

54. Management did not implement a proper records management system to maintain documents supporting reported performance information, assets, revenue and expenditure.
55. Systems and controls were not designed in a manner that would prevent, detect and address risks that had an impact on financial; performance and compliance reporting. In this regard, management did not ensure that regular, accurate and complete financial and performance reports that were supported and evidenced by credible information were prepared.

Governance

56. The municipality did not implement appropriate risk management activities to ensure that regular risk assessments, including the consideration of information technology risks are conducted adequately and that a risk strategy to address the risks is sufficiently monitored.

Other reports

57. I draw attention to the following engagements conducted by various parties that had, or could have, an impact on the matters reported in the municipality's consolidated and separate financial statements, reported performance information, compliance with applicable legislation and other related matters. These reports did not form part of my opinion on the consolidated and separate financial statements or my findings on the reported performance information or compliance with legislation.

58. At the request of the accounting officer and senior management, the internal audit unit performed numerous investigations on allegations received from the whistle-blower hotline. These investigations related to allegations of fraud, corruption, theft, mismanagement, recruitment and supply chain management (SCM) irregularities. During the 2016-17 financial year, thirty-one investigations were conducted. Of the thirty-one conducted, twenty-nine were concluded and reported to council. Two cases relating to SCM irregularities are still in progress at the date of this report.
59. The provincial department of Cooperative Governance and Traditional Affairs requested that an investigation be conducted after a senior staff member was suspended. The investigation commenced in May 2016 and covered the period 2012 to April 2016. The investigation was initiated based on an allegation of maladministration. This investigation has been completed and is pending legal advice.

Auditor General

Pietermaritzburg

19 December 2017



AUDITOR-GENERAL
SOUTH AFRICA

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